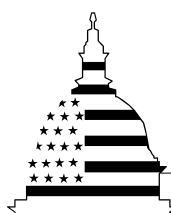


September 2003

FEDERAL HOME LOAN BANK SYSTEM

Key Loan Pricing Terms Can Differ Significantly



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Highlights

Highlights of [GAO-03-973](#), a report to the Ranking Minority Member, Senate Committee on Banking, Housing and Urban Affairs and the Chairman, Subcommittee on Capital Markets, House Committee on Financial Services

Why GAO Did This Study

The Federal Home Loan Bank System's (FHLBank System) traditional approach to providing community and housing finance through 12 regional FHLBanks (see figure) faces continual challenges due to consolidation in the financial services industry and the emergence of mortgage lenders with nationwide operations. In addition, the Federal Housing Finance Board (FHFB), the System's financial regulator, is analyzing the benefits and costs of potential changes to the System's membership rules that would make it easier for financial institutions to join multiple FHLBank districts (referred to as multidistrict membership). To provide information that would be helpful in assessing the potential safety and soundness implications of these developments, GAO was asked among other items to (1) determine whether key differences exist in the terms—such as interest rates and collateral requirements—that FHLBanks make on loans, also known as advances, to member financial institutions such as banks and thrifts and (2) discuss FHFB's oversight of the FHLBanks and safety and soundness data reporting requirements.

What GAO Recommends

GAO recommends that FHFB collect data necessary to monitor System safety and soundness. In written comments, FHFB and the FHLBanks agreed with GAO's recommendations.

www.gao.gov/cgi-bin/getrpt?GAO-03-973.

To view the full product, including the scope and methodology, click on the link above. For more information, contact William B. Shear at (202) 512-8678 or ShearW@gao.gov.

FEDERAL HOME LOAN BANK SYSTEM

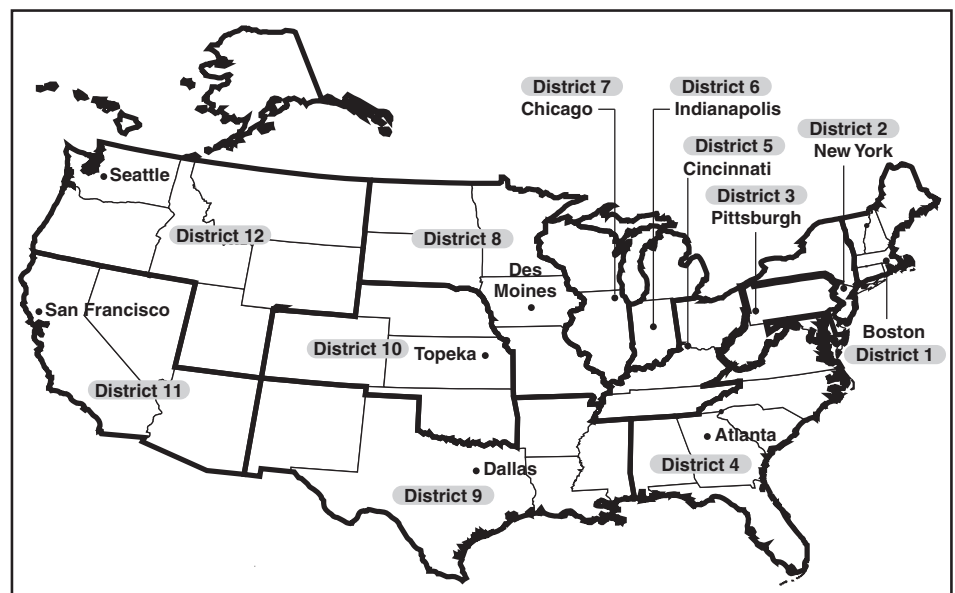
Key Loan Pricing Terms Can Differ Significantly

What GAO Found

Federal statutes and regulations require that the FHLBanks set advance interest rates above their borrowing costs and fully secure advances with eligible forms of collateral, such as single-family mortgage loans. However, within this framework, each of the 12 FHLBanks has independent authority to set advance pricing terms, which can result in several significant key differences among the banks. For example, due to differing costs and business strategies, FHLBank advance interest rates may differ and many FHLBanks charge lower interest rates based on advance size while others do not. Moreover, FHLBanks may set differing collateral requirements for their members. For example, one FHLBank allows its members to borrow up to 60 percent of the value of single family mortgages pledged as collateral to secure advances while another allows up to 85 percent.

Among the FHLBanks' differing approaches to setting advance pricing terms, FHFB has not found that any practice results in significant violations of statute or regulation. However FHFB also collects collateral data from the FHLBanks that have questionable value in their current format for monitoring the System's safety and soundness. Because FHLBank officials do not have clear information about how FHFB would like the data reported, the FHLBanks use different reporting definitions and criteria, which limits the data's analytical usefulness. Moreover, FHFB has not collected data necessary to assess the current extent of competition within the FHLBank System and the implications of holding companies with subsidiaries that operate in multiple FHLBank districts as well as multidistrict membership.

Locations of Federal Home Loan Banks



Source: FHFB.

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Abbreviations

CFI	Community Financial Institution
FDIC	Federal Deposit Insurance Corporation
FHLBank Act	Federal Home Loan Bank Act
FHLBanks	Federal Home Loan Banks
FHLBank System	Federal Home Loan Bank System
FHFB	Federal Housing Finance Board
GLBA	Gramm-Leach-Bliley Act
ORERC	Other Real Estate Related Collateral
MPF	Mortgage Partnership Finance
MPP	Mortgage Purchase Program
WAMU	Washington Mutual

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United States General Accounting Office
Washington, D.C. 20548

September 8, 2003

The Honorable Paul S. Sarbanes
Ranking Minority Member
Committee on Banking,
Housing, and Urban Affairs
United State Senate

The Honorable Richard H. Baker
Chairman, Subcommittee on Capital Markets,
Insurance, and Government Sponsored Enterprises
Committee on Financial Services
House of Representatives

The Federal Home Loan Bank System's (FHLBank System) traditional cooperative approach to providing housing and community finance through 12 regionally based Federal Home Loan Banks (FHLBank) faces continual challenges due to consolidation in the financial services industry and the emergence of mortgage lenders with nationwide operations. Traditionally, each FHLBank made loans, known as advances, that were secured by eligible collateral (e.g., single family mortgage loans) to member institutions—particularly thrifts—located in its district to support housing finance. However, many large bank and thrift holding companies now own subsidiaries located in various FHLBank districts. Each eligible subsidiary may join the FHLBank in which district its headquarters is located, and may obtain advances from that FHLBank.¹ Thus, these bank and thrift holding companies may, in effect, have access (through their subsidiaries) to advances from multiple FHLBanks.

¹Commercial banks, which may be owned by bank holding companies, were not allowed to join the FHLBank System until 1989.

Some observers have expressed concerns that these holding companies can pressure the FHLBanks to compete with one another on advance pricing terms—such as interest rates and collateral requirements—and that this competition could impair the overall safety and soundness of the FHLBanks, which were jointly and severally liable for \$710 billion in debt obligations as of June, 2003.² For example, the concern exists that a holding company could shift assets at a subsidiary located in one FHLBank district to pledge as collateral at a subsidiary in another district offering more favorable advance terms. Recently, these concerns have been heightened as the Federal Housing Finance Board (FHFB), the FHLBank System’s financial regulator, has analyzed the benefits and costs associated with potential changes to the System’s membership requirements that would allow financial organizations to join more than one FHLBank district (these potential changes to the System’s membership rules are commonly referred to as multidistrict membership).³ Supporters of multidistrict membership believe that it is necessary to modernize the FHLBank System’s structure, while critics believe that multidistrict membership would increase the potential for dangerous competition between the FHLBanks.

As discussed with your staff, this report provides an overview of advance term pricing requirements and practices within the FHLBank System that could be useful in assessing the extent of current competition among the FHLBanks and the potential competitive impacts of multidistrict membership. Specifically, you asked that we

1. describe the laws and regulations pertaining to the terms that FHLBanks can offer on advances;
2. provide information on whether key differences exist in current advance pricing and other terms across the FHLBanks;

²Joint and several liability means that, with respect to consolidated obligations, each FHLBank is responsible for its own debt obligations as well as the debt obligations of the other FHLBanks in the System. If one FHLBank experienced financial problems, and was unable to satisfy its repayment obligations, the other FHLBanks would be responsible for honoring them.

³Bank or thrift holding companies may establish separately chartered subsidiaries in two or more FHLBank districts. Under one concept of multidistrict membership, financial organizations—such as banks or thrifts—would be able to join multiple FHLBank districts without establishing separately chartered institutions.

-
3. determine whether holding companies face any legal or regulatory barriers in transferring assets among subsidiaries who are members of different FHLBank districts; and
 4. describe FHFB's safety and soundness oversight of the FHLBanks' advance pricing practices and review selected data that FHFB collects to monitor safety and soundness practices within the FHLBank System.

To address these objectives, we obtained and reviewed applicable federal laws and regulations pertaining to the terms that the FHLBanks can offer on advances. We also interviewed the 12 FHLBank presidents, credit and collateral staff from 7 of the 12 FHLBanks, and FHFB officials. We sent a set of structured questions to each of the 12 banks and reviewed their credit and collateral policies. In addition, we obtained and reviewed applicable laws and regulations regarding the transfer of funds and assets among holding companies and their subsidiaries, and interviewed representatives from the Federal Reserve Board and a large holding company. The scope of our work included a description of FHFB's examination program pertaining to advances but did not include an analysis of the program's effectiveness. However, we did analyze FHFB's collateral reporting requirements for the 12 FHLBanks. Because the information contained in this report is potentially sensitive, we generally do not identify individual FHLBanks in this report. Instead, we identify each of the 12 banks by the letters A-L. For each report table, we changed the individual FHLBanks identified by the letters A-L. Appendix I contains a detailed description of the scope and methodology of our work.

We conducted our review from January to September 2003 in Washington, D.C.; New York, New York; Topeka, Kansas; Dallas, Texas; Atlanta, Georgia; and Pittsburgh, Pennsylvania, and Indianapolis, Indiana, in accordance with generally accepted government auditing standards.

Results in Brief

The Federal Home Loan Bank Act (FHLBank Act), as amended by the Gramm-Leach-Bliley Act (GLBA), and FHFB regulations establish the general pricing and other terms that each FHLBank can offer on its advances to member institutions. The FHLBanks are required to set interest rates on advances above their borrowing costs and must also factor in administrative and other expenses. The FHLBank Act and GLBA also require that each FHLBank take the necessary steps to ensure that its loans are fully secured by eligible collateral. The eligible collateral includes cash, residential mortgages, government and agency securities, qualified nonagency mortgage-backed securities, other real estate related collateral (ORERC), and small business and agricultural loans or securities representing a whole interest in such loans held by community financial institutions (CFI).⁴

Within the framework established by statute and regulation for setting advance pricing terms and their independent authority within the FHLBank System, the FHLBanks have implemented several key differences in their policies, procedures, and practices. First, the FHLBanks have established sometimes differing formulas and business strategies to determine the interest rates to be charged on their advances. Moreover, some FHLBank officials told us that competition from other funding sources can influence advance interest rates, and some nationwide mortgage lenders play one FHLBank against another in an attempt to obtain favorable advance rates. Because of these differing business strategies and competitive pressures, available evidence indicates that there can be significant differences in stated advance rates among the FHLBanks for advances with comparable maturities. Many FHLBanks also charge different rates, depending upon the size of the advance, while others do not. Second, the FHLBanks have established differing collateral requirements for securing advances.

⁴Residential mortgages include single-family mortgages—defined as mortgages financing properties with 1-4 residential units—and multifamily mortgages. ORERC includes home equity loans and commercial real estate loans. Currently, CFIs are insured depository institutions with assets that do not exceed \$538 million. The asset size limit is adjusted annually for inflation and is based on a 3-year average of each institution's total assets.

For example, the FHLBanks may apply differing haircuts to the same types of collateral (for example, one bank applies a 40 percent haircut to the book value of single-family mortgage loans pledged as collateral, while another bank applies a 15 percent haircut).⁵ Third, the FHLBanks have established different advance borrowing capacity limits for their members; for example, 35 percent of a members' total assets at one FHLBank compared to 50 percent of assets at another. Fourth, although all 12 FHLBanks require their members to invest additional capital in the FHLBank based on their level of advances, the stock purchase requirements can differ (for example, from 3.5 percent of advances at one FHLBank to 5.0 percent at another).

Holding companies face few direct regulatory restrictions in transferring assets among their federally insured bank or thrift subsidiaries who are members of different FHLBank districts.⁶ Sections 23A and 23B of the Federal Reserve Act and Federal Reserve Regulation W and other federal laws do impose restrictions on certain transactions (for example, purchases of assets) between federally insured banks or thrifts and affiliated companies that are not insured so as to protect the financial condition of the insured institutions.⁷ However, Sections 23A and B and Regulation W and other federal laws generally exempt qualified insured banks or thrifts from these requirements when they engage in certain transactions with one another.⁸ According to Federal Reserve officials, these exemptions reflect the fact that under federal law, a federally insured institution within a holding company is generally liable for any losses

⁵Haircuts refer to the discounts that the FHLBanks apply to collateral that is pledged to secure advances. For example if the FHLBank has a 40 percent haircut for single-family mortgage loans, a member bank could borrow up to 60 percent of the value of the single-family mortgage loans that it pledged as collateral.

⁶Most members of the FHLBank System are separately chartered commercial banks or thrifts, which are insured by the Federal Deposit Insurance Corporation.

⁷Among other requirements, Section 23A imposes quantitative limits on covered transactions; for example, an insured bank's covered transactions with any single affiliate cannot exceed 10 percent of the bank's capital stock and surplus, and transactions with all affiliates combined cannot exceed 20 percent. Section 23B requires that certain transactions between insured banks and thrifts and uninsured affiliates take place on market terms.

⁸The exemption under 23A applies if the holding company owns or controls 80 percent or more of the voting securities of both insured institutions or if one insured institution owns or controls 80 percent of the voting securities of the other. Under 23B, transactions between a bank and a nonbank affiliate are restricted.

incurred by the Federal Deposit Insurance Corporation (FDIC) as a result of the failure of any other federally insured institution controlled by the holding company. The exemptions allow insured depository affiliates to conduct business with each other without needing to comply with financial restrictions with the understanding that the FDIC can offset its losses resulting from the failure of one or more insured depository affiliates by seizing the assets of insured affiliates that do not fail. Although few direct regulatory restrictions exist to transferring assets, holding companies may face other hurdles in transferring assets among their insured depository subsidiaries, such as meeting bank regulatory capital requirements or the stock purchase requirements of individual FHLBanks.⁹ We also note that the Federal Reserve has not quantified the extent to which transfers of assets among subsidiaries take place and it is not clear whether holding companies engage in such transfers to increase competitive pressures within the FHLBank System.

FHFB carries out its safety and soundness oversight responsibilities for the FHLBank System by conducting annual examinations and through off-site monitoring.¹⁰ In 2001 and 2002, FHFB examinations did not identify significant violations in the FHLBank's advance term pricing or collateral practices. However, we identified weaknesses in the data that FHFB collects from the FHLBanks, which could limit FHFB's ability to monitor current and emerging trends within the System. On an annual basis, FHFB requests that the FHLBanks provide data on collateral securing advances in order to, along with other items, exhibit the System's safety and soundness. Because FHLBank officials do not have clear information about how FHFB would like the data reported, the FHLBanks use different reporting definitions and criteria, which limits the data's analytical usefulness. Although FHFB officials said that FHFB examiners used the collateral data during the FHLBank examination process, the agency plans to study current data reporting and collection procedures. Moreover, FHFB has not collected data necessary to assess the current extent of competition within the FHLBank System and the implications of holding companies with

⁹Bank regulators, such as FDIC, impose capital requirements that apply to the insured subsidiaries of bank or thrift holding companies. In addition, each member of an FHLBank must purchase capital stock in that FHLBank. We do not address the potential application of state law to transfers of assets.

¹⁰Off-site monitoring involves FHFB headquarters staff reviewing financial data on the FHLBanks on a continual basis. Off-site monitoring can serve as an effective supplement to the annual examination process by, for example, identifying rapid changes in FHLBank financial risks and serving to assist examiners in planning examinations.

subsidiaries that operate in multiple FHLBank districts. By collecting data on, for example, the advance terms—such as interest rates—that holding company subsidiaries obtain from different FHLBanks, FHFB would be in a better position to (1) determine whether competition may affect FHLBank safety and soundness and (2) assess the potential impacts of multidistrict membership.

To strengthen its oversight capacity for the FHLBank System, we recommend that FHFB review the effectiveness of its current collateral data collection program and work with the FHLBanks to obtain data that are useful in assessing practices within the System. We also recommend that FHFB work with the FHLBanks to collect data necessary to assess the potential effects of competition on the safety and soundness of the FHLBank System.

We provided a draft of this report to FHFB, the FHLBank Presidents' Conference, and the Board of Governors of the Federal Reserve System for their review and comment. We received written comments from FHFB and the FHLBank Presidents' Conference—which are reprinted in appendixes III and IV—and technical comments from these organizations and the Federal Reserve, which have been incorporated where appropriate. FHFB agreed with the recommendations in the draft report that it review its data collection and reporting procedures to assess the FHLBanks collateral practices and competition within the System. The FHLBank Presidents' Conference commented that statutes and regulations allow individual FHLBanks to set advance pricing terms that allow the banks to meet the needs of their members while continuing to operate in a safe and sound manner. The Conference also said that they would work with FHFB to collect revised collateral data.

Background

Established in 1932, each FHLBank is a government-sponsored enterprise (GSE) that is cooperatively owned by its members (see fig. 1 for the location of the 12 FHLBanks). The 12 FHLBanks, along with the Office of Finance (which issues debt on behalf of the FHLBanks), comprise the FHLBank System. The members of each FHLBank must buy stock in the FHLBank as a prerequisite for obtaining advances and other FHLBank services. FHLBank System assets consist of advances and investments, such as money market funds and mortgage-backed securities (see table 1). In addition, FHLBank assets consist of acquired mortgages that the FHLBanks purchase from their members under the Mortgage Partnership Finance (MPF) program or Mortgage Purchase Program (MPP).¹¹ The FHLBank-purchased mortgages consist of both conventional mortgages and federally insured and guaranteed mortgages.¹²

¹¹“Mortgage Partnership Finance” and “MPF” are registered trademarks of the FHLBank of Chicago.

¹²Conventional mortgages do not have federal insurance or guarantees. FHLBank acquired mortgages are below the conforming mortgage loan limit, which is currently \$322,700 for single-family properties. Fannie Mae and Freddie Mac, the other two housing GSEs, also purchase conventional conforming mortgages and issue mortgage backed securities.

Figure 1: Location of the 12 Federal Home Loan Banks



Source: FHFB.

Table 1: FHLBank System Assets, as of June 30, 2003

Dollars in billions				
Advances	Mortgages	Investments	Other^a	Total assets
\$506	\$90	\$206	\$7	\$809

Source: Office of Finance.

^aThese assets include interest bearing deposits and federal funds sold.

The FHLBank System raises funds in the capital markets partially on the strength of its ties to the federal government. Due to these ties, investors perceive an implied guarantee by the federal government on the System debt based on the belief that the government would come to the rescue of the FHLBank System rather than allow it to default on its obligations in the event of severe financial difficulties. The primary source of funds for the FHLBank System is the issuance of debt securities known as consolidated obligations, through its Office of Finance, which stood at \$710 billion as of June 30, 2003. Consolidated obligations are the “joint and several” obligations of the FHLBanks and all of the banks may be required to cover such obligations of another bank that defaults on its repayment obligations. Under the joint and several structure, the potential for moral hazard exists. That is, FHLBanks may have incentives to take financial risks knowing that their losses would be covered by other FHLBanks or, ultimately, the federal government. Federal statutes and regulations as well as FHFB’s oversight efforts—which are discussed in this report—are designed to help ensure that the FHLBanks conduct their business in a safe and sound manner.

The FHLBank Act provides that an eligible institution may become a member only of the FHLBank district in which its principal place of business is located, or an adjoining district for convenience purposes and if approved by FHFB. However, bank or thrift holding companies may own subsidiaries in two or more FHLBank districts and each eligible subsidiary may become a member of its district FHLBank. To become a FHLBank member, each subsidiary must be a separately chartered institution, such as a national bank or state-chartered bank or thrift. According to FHFB, approximately 100 bank or thrift holding companies currently operate in two or more FHLBank districts by having established separately chartered subsidiaries in those districts.

In 2000 and 2001, continuing a long standing trend, several holding companies with subsidiaries that operated in two or more FHLBank districts merged with or purchased financial institutions that were also

members of FHLBank districts. These holding companies sought to consolidate the merged or purchased institutions under one existing charter and did not want to maintain separately chartered institutions. For example, Washington Mutual (WAMU)—a thrift holding company with subsidiaries in the Seattle, San Francisco, and Topeka FHLBank districts—purchased Bank United, a member of the Dallas FHLBank district, and Dime Savings, a member of the New York FHLBank district. WAMU chose not to maintain separate charters for Bank United and Dime Savings for business purposes and instead decided to merge the institutions into its existing subsidiaries. However, under FHFB regulations Dime Savings and Bank United could no longer remain members of the FHLBank System and could no longer obtain new advances or other services from the FHLBank of Dallas and the FHLBank of New York. Therefore, WAMU was required to pay back Bank United and Dime Savings' outstanding balances under their original terms.

In 2000, the FHLBank of Dallas submitted to the FHFB an application (which the FHFB subsequently treated as a petition) to grant approval to WAMU's thrift subsidiary's application for membership in the FHLBank of Dallas while maintaining its membership in the FHLBank of San Francisco (the petition has been referred to as advocating multidistrict membership). The Dallas FHLBank filed the petition under the "demanded by convenience" standard.¹³ After the initial petition, FHFB received similar requests from three other FHLBanks, requests to intervene, and comment letters both in favor and against.¹⁴ Given the controversy associated with these petitions and their potential effects on the System (including the potential for increased competition among the FHLBanks), FHFB did not act on them and, in October 2001, requested comments from the public on the petitions. In 2002, FHFB obtained a legal opinion from a law firm stating that it had the legal authority, under certain conditions, to approve

¹³The FHLBank of Dallas requested that the WAMU thrift subsidiary belong to both the San Francisco and Dallas districts. FHLBank Dallas interpreted the phrase in the FHLBank Act stating that a member can join the district where it is headquartered or an adjoining district if demanded by convenience as meaning the WAMU subsidiary could join both districts without establishing a separately chartered subsidiary in Dallas. Traditionally, the phrase has been understood to mean a FHLBank member can join either the district where it is headquartered or the adjoining district, but not both.

¹⁴A member, FHLBank, or the Office of Finance may file a request to intervene in the consideration of the petition, in support or against, if it believes its rights may be affected. These requests must include a statement of the facts, a description of the relief requested, and be filed with the Secretary to the Federal Housing Finance Board within 45 days from the date the petition is filed.

multidistrict membership under its broad safety and soundness regulatory authority and requested that the 12 FHLBanks answer questions related to multidistrict membership, which the FHLBanks did by February 2003. During 2003, FHFB staff, at the direction of the agency's chairman, analyzed the benefits and costs associated with multidistrict membership.

Statutes and Regulations Establish the General Pricing and Other Terms Each FHLBank Can Offer on Advances to Member Institutions

The FHLBank Act, as amended by GLBA, and FHFB regulations establish the general pricing and other terms that each FHLBank can offer on its advances.¹⁵ Statutory and regulatory provisions establish requirements for FHLBank pricing on advances, allow for price differentiation at the FHLBanks, require that advances must be fully secured, and establish eligible types of collateral. FHFB regulations establish more specific requirements to help ensure that the FHLBanks conduct their advance business in a safe and sound manner.

General Requirements for Terms on Advance Pricing

According to FHFB regulations issued pursuant to the FHLBank Act, FHLBank advances may not be priced below the marginal cost to the FHLBank of raising matching term and maturity funds in the marketplace, including embedded options, plus the administrative and operating costs associated with making advances.¹⁶ FHLBanks are allowed to differentiate in advance prices based on the FHLBank's assessment of the credit and other risk of lending to any particular member, or other reasonable criteria.

¹⁵Section 7(j) of the FHLBank Act (12 U.S.C. 1427(j)) requires that each Bank's board of directors administer the affairs of the Bank "fairly and impartially and without discrimination in favor of or against a member," and section 9 of the FHLBank Act (12 U.S.C. 1429) provides that a Bank "may at its discretion deny any such application (for an advance) or may grant it on such conditions as the (Bank) may prescribe."

¹⁶12 C.F.R. 950.5(b)(1).

Per FHFB's guidance, such differentiation could include providing discounts to members based on the volume of the advance.¹⁷ Each FHLBank is to include in its member products policy standards and criteria for differential pricing and is to apply its standards and criteria consistently and without discrimination to all members.

The FHLBank Act, as amended by GLBA, requires that FHLBanks fully secure their advances with eligible collateral. The eligible collateral, as listed in table 2, ranges from whole single family mortgages to small business and agricultural loans.¹⁸ GLBA, which amended the FHLBank Act, expanded the collateral that member institutions could use to secure an advance. In particular, GLBA allowed CFIs, those FHLBank System members that are FDIC insured depository institutions that currently have \$538 million or less in total assets, to pledge small business and agricultural loans as collateral. GLBA allowed CFIs to use the expanded collateral categories because some small institutions lacked a sufficient quantity of other types of assets—such as mortgage loans—necessary to secure FHLBank advances. GLBA also allowed all FHLBank members to make greater use of ORERC—such as commercial real estate loans and home equity loans—as collateral for advances. The FHLBanks may restrict the types of eligible collateral available to them as security, based upon the creditworthiness or operations of the borrower, the quality of the collateral, or other reasonable criteria.

¹⁷According to the preamble to the final rule on advances, published May 20, 1993, 58 FR 29456, the Board concluded that the extension of credit to FHLBank members based on the member's creditworthiness, or other reasonable criteria applied equally to all members, does not constitute "discrimination" under 7(j) of the FHLBank Act. The Board also approved risk based pricing, stating, "risk based pricing of advances should enhance the fairness of the Banks' credit programs, since the terms of advances to more creditworthy members should be more favorable than those to members posing a greater credit risk to a Bank." In addition, the Board approved of differential pricing of advances based upon criteria other than risk, subject to the application of consistent standards to all borrowing members. The preamble cited the fact that "certain Banks have offered 'volume discounts' to members who finance a certain percentage of their total assets with Bank advances," as an example of allowable differential pricing. 1993 WL 167293 (F.R.)

¹⁸Single-family mortgages are mortgages on dwellings that include condominiums, planned unit developments, townhomes, and qualified mobile homes affixed to the land. The FHLBanks typically prefer that these mortgages are on owner-occupied dwellings.

Table 2: Types of Eligible Collateral in the FHLBank System

1.	Fully disbursed, whole first single-family or multifamily mortgages on improved residential property (not more than 90 days delinquent), or securities representing a whole interest in these mortgages.
2.	Securities issued, insured, or guaranteed by the United States or a U.S. agency, including mortgage-backed securities issued by Fannie Mae or Freddie Mac. ^a
3.	Cash or deposits at a FHLBank.
4.	Other real estate related collateral, such as home equity loans or commercial real estate, acceptable to the FHLBank and subject to certain conditions.
5.	Secured loans for small business, agriculture, or securities representing a whole interest in such secured loans, in the case of any CFI.

Source: FHLBank Act as amended.

^aAs part of their business activities, Fannie Mae and Freddie Mac issue mortgage-backed securities.

By fully securing advances with eligible collateral as required by the FHLBank Act, FHLBanks can protect their interests should one or more of their members fail. Typically, FHLBanks make advances on what is known as a blanket lien; that is, the FHLBank has the authority to take control of all the assets that are eligible as collateral on a member's books. In cases in which an FHLBank determines that a member is experiencing financial difficulty, the FHLBank may require the member to list specific assets that are securing advances or may even require the member to deliver the collateral to the FHLBank.¹⁹ Should the member fail, the FHLBank can sell the pledged collateral to ensure repayment of principal and the interest on the advance. Due in part to the collateralization requirements, the FHLBank System has never experienced a loss on an advance.

FHFB Regulations Establish Additional Advance Term Requirements

FHFB has issued several regulations that are designed to help ensure that the FHLBanks make advances in a safe and sound manner. For example, FHFB has established regulations pertaining to the use of ORERC and small business and agricultural loans as collateral, which are generally considered riskier than other forms of collateral, such as single-family mortgages. FHFB regulations require that FHLBanks can reliably discount the value of ORERC and small business and agricultural loans pledged as collateral. Under its regulations, FHFB also has the authority to require an

¹⁹Many FHLBanks also have several non financial triggers that require specific listing or delivery of assets that are pledged as collateral.

FHLBank to increase its standards for all forms of eligible collateral. FHFB requires through regulation that FHLBanks take the necessary steps to ensure that collateral is secure and to establish written procedures for verifying the existence of collateral.

Significant Differences Exist in Key Advance Pricing Terms among the FHLBanks

Although the FHLBank Act and FHFB regulations establish the advance pricing framework, each FHLBank has independent authority within the framework to establish specific policies and procedures to meet its business and member requirements. Our review of key advance pricing terms—advance interest rates, collateral requirements, advance borrowing capacity, and capital stock purchase requirements—identified several significant differences among the 12 FHLBanks. The FHLBanks may charge different interest rates on advances with comparable maturities, some may establish interest rates on the basis of advance size while others do not, and the FHLBanks apply differing haircuts to the same type of collateral, establish different borrowing limits, and require members to purchase FHLBank stock in differing amounts depending upon their levels of advances outstanding.

Advance Interest Rates May Vary Based on FHLBank Operating Costs, Business Strategies, and Competition from Other Sources

The process of setting advance interest rates can depend on several key factors, including cost of funds, operating expenses, business strategies, and competition from other sources, and may differ from one FHLBank to another. In general, each FHLBank attempts to set advance interest rates at a level that covers its costs—including cost of funds and operating expenses—while allowing for the payment of a reasonable rate of return (typically through the payment of dividends) to member institutions. Although the FHLBanks generally have the same cost of funds because they borrow through the Office of Finance, they may have different operating expenses to administer their advance business.²⁰ Moreover, the business strategies adopted by individual FHLBanks may also influence the advance interest rates that they charge to members. In particular, FHLBank officials said that there can be a connection between the advance interest rate that they charge and the dividend rate that they pay. That is, an FHLBank choosing to pay a relatively high dividend may need to charge a relatively high advance rate to earn sufficient profits to cover the costs

²⁰Total FHLBank System operating expenses of \$396 million are very small compared to other expenses, such as interest expenses, which totaled nearly \$18 billion in 2002.

associated with the dividend. In contrast, other FHLBanks may decide to provide value to their members through lowering their advance rates, which may mean a decrease in their dividend. Table 3 shows that some FHLBanks consistently pay higher dividends than others. For example, Bank E paid an average dividend of 7.63 percent from 1997 through 2002, which was 250 basis points higher than the average dividend of Bank L over the same period.

Table 3: FHLBanks' Average Annual Dividend Rates, 1997-2002

FHLBanks	1997	1998	1999	2000	2001	2002	Average	Rank
A	6.1	5.76	5.36	7.17	5.99	5.45	5.97	10
B	6.82	6.63	6.69	7.38	6.34	5.25	6.52	6
C	6.48	6.4	6.54	7.63	5.87	3.68	6.10	9
D	7	6.63	6.3	6.92	4.45	3	5.73	11
E	7.99	8.01	8	8.25	7.44	6.06	7.63	1
F	7.25	7.38	7.13	8.03	6.78	4.56	6.86	4
G	6.6	7.25	6.8	6.95	6.29	4.51	6.40	7
H	7.19	7.19	7.06	7.34	6.75	4.63	6.69	5
I	7.69	7.69	7.36	6.5	6.88	5.98	7.02	2
J	6.38	6.5	6.63	7.06	6.5	3.56	6.11	8
K	7.25	7.44	7.56	7.75	6.75	5.31	7.01	3
L	5.95	5.92	5.5	6.36	4.13	2.94	5.13	12

Source: FHLBanks.

Note: The A-L listing of the FHLBanks in this table differs from the A-L listings in other tables in this report.

FHLBank business strategies involving other assets—such as mortgage purchase programs and other investments—may also influence the interest rate that they charge on advances. For example, the potential exists that the degree to which an FHLBank participates in the MPP or the MPF program would affect its advance interest rate. If an FHLBank commits substantial resources to the MPP or the MPF program, it may use any profits earned to offset the advance interest rate or it may use funds earned from advances to support the MPP or MPF program. Or, the FHLBank could use the profits to pay a higher dividend and leave advance rates unchanged or some combination thereof. Available evidence suggests that there is wide variation within the FHLBank System on the extent to which individual banks participate in the asset purchase programs. For example, more than 46 percent of the assets at one FHLBank now consist of acquired

mortgages while the ratio is only 1.5 percent at another FHLBank. Similarly, FHLBanks could also increase investments in other types of assets, such as mortgage-backed securities, and use the income derived to offset advance interest rates or pay a higher dividend.

Some FHLBank officials told us that competition from other sources can also influence the interest rates that they charge on advances. For example, officials said that they monitor other financial markets—such as the repo market—to determine how competitive their advance rates are with other funding sources.²¹ In addition, some FHLBank officials said that competition may also arise from the advance interest rates and other terms offered by other FHLBanks. The officials said that large bank or thrift holding companies that have subsidiaries in multiple FHLBank districts sometimes play one FHLBank against another in an attempt to obtain more favorable advance pricing terms. Some FHLBank officials said that they will adjust their advance interest rates within established parameters to ensure that their rates are competitive with other sources of funds. An individual FHLBank's willingness to compete with other fund providers could influence differences in advance rates across the FHLBanks.

Given the variety of factors that may be involved in setting advance interest rates, we are unable to explain completely why individual FHLBanks charge the rates that they do. Nevertheless, limited available data indicate that these factors result in sometimes significant differences in interest rates on advances with comparable maturities. Table 4 shows the advance interest rates for eleven FHLBanks on June 10, 2003 (the other FHLBank stated that its advance interest rate data were proprietary). The differences between the lowest and highest interest rates can be significant. For example, for an advance of 12 months, the difference between Bank H and D was 36 basis points.

²¹A repurchase agreement, commonly referred to as a “repo,” is a transaction in which a dealer in effect borrows money by selling securities and simultaneously agreeing to buy them back at a higher price at a later time.

Table 4: Comparison of Selected FHLBank Interest Rates on Fixed Rate Advances (June 10, 2003)^a

Term	Bank A	Bank B	Bank C	Bank D	Bank E	Bank F	Bank G	Bank H	Bank I	Bank J	Bank K	Range	Difference in basis points
12 mo.	1.16	1.29	1.10	1.43	1.37	1.29	1.22	1.07	1.31	1.3	1.41	1.07-1.43	36
24 mo.	1.42	1.45	1.35	1.62	1.58	1.51	1.46	1.36	1.56	1.55	1.62	1.35-1.62	27
36 mo.	1.75	1.82	1.74	1.92	2.01	1.88	1.79	1.71	1.91	1.9	1.95	1.71-2.01	30
48 mo.	2.16	2.27	2.18	2.39	2.42	2.27	2.21	2.21	2.39	2.3	2.36	2.16-2.42	26
60 mo.	2.53	2.58	2.53	2.71	2.79	2.63	2.58	2.55	2.74	2.66	2.72	2.53-2.79	26

Source: Selected FHLBanks.

Note: The A-K listing of the FHLBanks in this table differs from the alphabetic listings in other tables in this report.

^aThe interest rates shown are generally for regular fixed term and rate advances with no discounting. We also obtained advance interest rate data from the FHLBanks on July 18 and 25, 2003 to replicate our results (see app. II). The FHLBanks also differ in their policies regarding payment frequency and daycount accrual methods. No attempt is made here to harmonize the data to a single payment frequency and daycount accrual standard.

Due to our reporting deadlines, the scope of our work did not involve obtaining comparable historical data on the advance interest rates charged by individual FHLBanks. We obtained the data from the Web sites of nine FHLBanks while two other FHLBanks provided the data separately. One FHLBank stated that its advance interest rate data were proprietary. Of the nine FHLBanks that do publish advance interest rate data on their Web sites, some publish historical data while others do not. Of banks that do report historical rate data, some use different and incomparable reporting methodologies. Additionally, the FHLBanks reserve the right to negotiate with members on advance interest rates; therefore, the advance interest rates posted on the FHLBanks Web sites may or may not be the rate paid by all members.

Most FHLBanks Offer Discounts on Advance Rates Based on Volume

Our review indicates that eight FHLBanks have established specific programs that offer volume-driven advance rate discounts, while four others have not established such programs (see table 5). Under these programs, also referred to as tiered pricing, the FHLBank may reduce the standard interest rate charged on advances depending upon the size of the advance. The programs operate similarly as each passes on to members the economies of scale the FHLBanks realize from high-volume transactions. However, as table 5 illustrates, the number of pricing tiers at each FHLBank varies; three banks have established two tiers, two banks have established three tiers, two banks have established four tiers, and one bank states that it provides volume-driven discounts. The basis point discounts that the FHLBanks offer on volume driven discounts can also vary. For example, one FHLBank reduces its advance rates 15 to 20 basis points for advances over \$25 million, while another FHLBank reduces its advance interest rates 6 to 12 basis points.

Table 5: Tiered Advance Pricing Programs at the FHLBanks

FHLBanks	Tiered pricing (Y/N)	Tiered pricing program descriptions
Bank A	No	
Bank B	Yes	2 Tiers: Advances under \$25 million Advances over \$25 million
Bank C	No	
Bank D	No	
Bank E	Yes	Volume discounts on large advances
Bank F	Yes	2 Tiers: Advances under \$10 million Advances \$10 million and over
Bank G	Yes	2 Tiers: Advances under \$25 million Advances \$25 million and over
Bank H	Yes	4 Tiers: Advances \$5-24 million Advances \$25-49 million Advances \$50-99 million Advances \$100 million and over
Bank I	Yes	4 Tiers: Advances under \$10 million Advances \$10-24 million Advances \$25-99 million Advances \$100 million and over
Bank J	Yes	3 Tiers: Advances under \$5 million Advances \$5-25 million Advances over \$25 million
Bank K	Yes	3 Tiers: Advances for less creditworthy members required to deliver collateral Advances under \$10 million (standard pricing tier) Advances over \$10 million
Bank L	No	

Source: FHLBanks.

Note: The A-L listing of the FHLBanks in this table differs from the A-L listing in other tables in this report.

FHLBank officials said that their large members are the primary beneficiaries of the tiered pricing programs because they have the capacity to borrow in large volumes. However, officials from two FHLBanks also said that they will aggregate advance requests from smaller members so that they can benefit from volume-driven rates as well. Representatives from several FHLBanks, including those that do not have tiered pricing programs, said that they also periodically offer “special deals” on advance rates to all of their members. If a FHLBank, for example, obtains favorable borrowing costs, it may pass these savings on to its members through special deals that are announced by fax or e-mail.

With respect to the four FHLBanks that do not have specific tiered pricing programs, officials said that they preferred to offer the same advance rate to all members. Although these FHLBanks do not have specific tiered pricing programs based on volume, they may differentiate in price in other ways. For example, one FHLBank offers standard rates on all advances requested by telephone but offers specified discounts on advance requests made through its secured Web site. Officials from this bank said that more than 98 percent of its advances are made through the Web site. Banks that do offer tiered pricing programs may also offer differing advance rates on the basis of the creditworthiness of their members. For example, one FHLBank has established 10 separate categories that have different interest rates and collateral requirements depending upon a member's creditworthiness. This FHLBank, as do other FHLBanks, establishes members' creditworthiness through, among other steps, reviewing publicly available financial information and conducting on-site visits to review collateral management practices.

We also note that analyzing the FHLBanks' tiered pricing programs was difficult, because the programs are not fully transparent as some banks "negotiate" prices with larger members. Some FHLBank officials said that larger members periodically request advance terms that differ from posted rates and that FHLBank representatives do have some authority to customize deals. For example, officials at one FHLBank said that its representatives had the authority to negotiate the stated advance interest rates. None of the FHLBank officials we contacted said that they had authority to negotiate based on collateral standards. Some FHLBank officials said that they notify their members of the terms of negotiated transactions whenever they take place (for example, by e-mail). Other FHLBank officials said that they will make the terms of negotiated deals available only when another member requests an advance with similar features.

FHLBanks Have Established Sometimes Differing Collateral Requirements for Securing Advances

The FHLBanks may also apply differing haircuts to collateral pledged by member institutions to secure advances. Table 6 shows the haircuts that the FHLBanks apply under their blanket liens to single-family mortgage collateral, which is considered one of the most secure forms of collateral. Several FHLBanks apply a range of haircuts to single-family collateral (for example, FHLBank C) based on their assessments of the credit risk of the collateral. For those banks that apply one haircut to single-family collateral, the haircut differences can be significant. For example, a member could borrow up to 85 percent of its pledged single-family

collateral at FHLBank L (which has a 15 percent haircut) but only up to 60 percent at FHLBank J (which has a 40 percent haircut). We note that the FHLBanks have established other advance borrowing limits for their members, which are discussed in the next section.

Table 6: FHLBank Haircuts for Single-Family Mortgage Collateral under the Blanket Lien Option

FHLBanks	Collateral haircut^a
Bank A	9 -20% ^b
Bank B	20% ^c
Bank C	20-43% ^d
Bank D	17%
Bank E	25%
Bank F	25% or more
Bank G	17-44% ^e
Bank H	31 or 40% ^f
Bank I	31%
Bank J	40%
Bank K	25%
Bank L	15%

Source: FHLBanks.

Note: The A-L listing of the FHLBanks in this table differs from the A-L listing in other tables in this report.

^aThe FHLBanks use different methods to reflect the percentage haircut requirement on collateral. We have converted their different measures to one consistent standard for purposes of comparison. Eleven of the 12 FHLBanks generally apply haircuts to the book value of eligible collateral, while one has established a methodology to apply haircuts to the fair market value of the collateral.

^bHaircut depends upon the creditworthiness of the member.

^cBank determines fair market value of collateral. The Bank will use "book value" as fair market value for nondelivered, nonsecurities collateral where a fair market value estimate is unavailable.

^dRange depends on a creditworthiness assessment rating.

^eThe haircut depends upon the relative riskiness of the collateral.

^fAmount reflected is for reviewed loans that have either an adjustable rate (31%) or a fixed rate (40%).

Our review also identified other differences in the FHLBanks collateral standards. For example, we found that several FHLBanks require or prefer their members to pledge all of their single-family mortgages as collateral before they will consider the use of other types of collateral—such as ORERC or small business and agricultural loans—to secure advances. In contrast, other FHLBanks allow members to pledge any form of eligible collateral—such as commercial real estate loans—to secure advances without requiring that other types of eligible collateral be used first.

Borrowing Capacity Limits Vary Across the FHLBanks

To minimize the risks associated with making advances to their members, the FHLBanks have also established borrowing capacity limits, which can vary. Table 7 shows that three FHLBanks allow their members to obtain advances equal to the value of all their eligible collateral after appropriate haircuts have been applied. These FHLBanks borrowing limits do not include a specific limit on the ratio of advances to a member's total assets as is the case at the other nine banks. Of the nine banks with specific ratio limits, the borrowing limits vary to some extent; for example, one FHLBank sets total advance borrowings at 35 percent of a member's assets. Other FHLBanks may allow members to borrow up to 50 percent of their total assets without board approval and, in one case, up to 55 percent if approved by the bank president. The borrowing capacity of individual members is determined on a case-by-case basis depending on the creditworthiness of the member and the member's collateral.

Table 7: FHLBank System Borrowing Capacity Limits

FHLBank	Member bank borrowing capacity (BC) limits^a
Bank A	Total eligible collateral after appropriate discounts.
Bank B	40 percent of total assets. Financial status may dictate a lower BC.
Bank C	Total eligible collateral multiplied by appropriate haircut, minus the member bank's obligations.
Bank D	40 percent of total assets, up to 55 percent if approved by the bank president.
Bank E	50 percent of member's total assets. Financial status and/or collateral requirements may dictate a higher/lower BC.
Bank F	Overall credit exposure to total assets may not exceed 50 percent. Bank may apply additional borrowing limits as applicable.
Bank G	Bank assigns borrowing capacity percentage to eligible collateral.
Bank H	50 percent of a member's total assets, higher with consent of the board.
Bank I	Total eligible (unpledged) collateral after appropriate haircuts.
Bank J	40 percent of total assets.
Bank K	50 percent of adjusted assets (member's assets minus borrowings from all sources).
Bank L	Under blanket lien, total secured borrowings must be less than 35 percent of total assets. Single-family mortgage loans should equal at least 10 percent of total assets.

Source: FHLBank policy manuals and interviews with FHLBank officials.

Note: The A-L listing of the FHLBanks in this table differs from the A-L listing in other tables in this report.

^aCapacity limits established by banks are always subject to the amount of eligible collateral held by a member.

FHLBanks Require Members to Purchase Different Amounts of Capital Stock Depending upon Advance Activity

FHLBanks have also established activity based stock purchase requirements for advances, which can differ (see table 8).²² As the table indicates, the specific capital ratio requirements can differ; for example, FHLBank L has a 3.5 percent stock purchase requirement while FHLBank G has a 5 percent requirement.

Table 8: FHLBanks’ Advances Activity Based Stock Purchase Requirements

FHLBank	Capital requirement ^a
A	4.7%
B	4.75%
C	4.5%
D	2 – 4% ^b
E	4.5%
F	4.25%
G	5%
H	4.5%
I	4.45%
J	4.5%
K	5%
L	3.5%

Source: FHLBanks.

Note: The A-L listing of the FHLBanks in this table differs from the A-L listing in other tables in this report.

^aFHFB has approved new capital plans for all 12 FHLBanks. These plans include the capital requirements for each of the FHLBanks. The table reflects the approved capital requirements of the 12 FHLBanks. As of the time of this report, 5 banks have implemented their new requirements. The FHLBank boards of directors set ranges of capital to advances ratios, and then choose a specific ratio of capital stock that members are required to meet when taking out advances. Only the specific ratios are shown in the table.

²²These activity based capital requirements are in addition to minimum membership requirements for being a member of a FHLBank. Each FHLBank requires its members to invest capital based on the amount of advances they have outstanding. FHLBank boards of directors typically set ranges of capital to advances ratios. FHLBank boards of directors also typically set specific ratios within the range that members are required to meet when taking out advances. Members must comply with the activity-based requirement as long as the relevant activity remains outstanding, including periods beyond the termination of the member’s membership in a FHLBank. The advances investment requirements are calculated daily and each time a member enters into a new advances transaction.

^bThe FHLBank's advance activity capital requirement range of 2 to 4 percent has been set by its board within a larger range of 1 to 6 percent. The capital requirement within the 2 to 4 percent range is based on the extent of the excess stock held by each member and the FHLBank at any particular point in time. The member may use (borrow) FHLBank excess stock under certain conditions rather than purchase additional stock, which could make the FHLBank overcapitalized.

Holding Companies Can Generally Transfer Funds and Assets among Their Insured Subsidiaries

Although Section 23A and 23B of the Federal Reserve Act and Regulation W impose restrictions on the transfer of assets among some subsidiaries of holding companies, these restrictions generally do not apply to transfers of assets between depository institution subsidiaries that are federally insured.²³ Accordingly, each of the more than 100 holding companies that have federally insured bank or thrift subsidiaries that are members of various FHLBank districts may be able to transfer assets among their insured depository subsidiaries with few restrictions under specified conditions. However, holding companies may face some hurdles—such as managing their balance sheets or meeting capital requirements—when transferring assets from one insured subsidiary to another. We also note that the Federal Reserve has not quantified the extent to which transfers of assets among subsidiaries take place, and it is not clear whether holding companies engage in such transfers to increase competitive pressures within the FHLBank System.

Sections 23A and 23B of the Federal Reserve Act Limit Transactions between Affiliates

Sections 23A and 23B of the Federal Reserve Act set limits on covered transactions between a depository institution and its affiliates.²⁴ Sections 23A and 23B are designed to protect against a depository institution suffering losses in transactions with affiliates. They limit the ability of a depository institution to transfer to its affiliates the subsidy arising from the institution's access to the federal safety net, including the deposit insurance funds. Under section 23A, a bank's affiliates include, among

²³12 U.S.C. 371c, 12 U.S.C. 371c-1 and 12 C.F.R. Part 223. Section 11(a)(1) of the Home Owners' Loan Act, 12 U.S.C. 1468(a)(1), generally applies sections 23A and 23B of the Federal Reserve Act to every savings association in the same manner and to the same extent as if the savings association were a member bank of the Federal Reserve System. The Office of Thrift Supervision has issued proposed regulations on transactions with affiliates that reflect Regulation W.

²⁴A "covered transaction" is defined as a loan or extension of credit to an affiliate, the purchase of or investment in securities issued by an affiliate, the purchase of assets from an affiliate, acceptance of securities issued by an affiliate as collateral security for a loan or extension of credit, issuance of a guarantee, acceptance, or a letter of credit on behalf of an affiliate.

other companies, any companies that control the bank, any companies under common control with the bank, and certain investment funds that are advised by the bank or an affiliate of the bank. Affiliate has the same meaning under 23B as the meaning given under 23A, except that the term affiliate under 23B does not include an insured bank or an insured savings association.

According to Section 23A, a bank's covered transactions with any single affiliate cannot exceed 10 percent of the bank's capital stock and surplus, and transactions with all affiliates combined cannot exceed 20 percent of the bank's capital stock and surplus. All transactions between a bank and its affiliates must be on terms and conditions that are consistent with safe and sound banking practices, and a bank cannot purchase low quality assets from its affiliates. Finally, section 23A requires that a bank's extensions of credit to affiliates and guarantees on behalf of affiliates be appropriately secured by a statutorily defined amount of collateral. Section 23B requires that certain transactions between a bank and its affiliates occur on market terms. This is defined to mean that the transaction must take place on terms and under circumstances that are substantially the same, or at least as favorable to the bank, as those prevailing at the time for comparable transactions with unaffiliated companies.

Transactions that are covered by 23A and 23B include (1) purchases of assets by a bank from an affiliate, (2) extensions of credit by a bank to an affiliate, (3) investments by a bank in securities issued by an affiliate, (4) guarantees by a bank on behalf of an affiliate, and (5) certain other transactions that expose the bank to an affiliate's credit or investment risk. Section 23B also applies to any sale of assets by the bank to an affiliate, any payment of money or furnishing of services by the bank to an affiliate, and any transaction by the bank with a third party if an affiliate has a financial interest in the third party or in an affiliate that is a participant in the transaction.

Sister Banking Exemption Allows Transfer of Assets among Subsidiaries of Bank and Thrift Holding Companies

Section 23A exempts several types of transactions from certain aspects of the statute. One exemption, known as the Sister Bank Exemption, exists for transactions between a bank or thrift and another bank or thrift if a company controls 80 percent or more of the voting securities of both banks or thrifts or if one bank controls 80 percent or more of the voting securities of the other. The exemption applies only to transactions between insured depository institutions. Because Section 23B exempts banks and thrifts from its definition of affiliate, sister banks (those banks that qualify for the exemption) are also exempt from the requirement that transactions between insured banks or thrifts and their affiliates be conducted on an arm's length basis. According to the Federal Reserve, these exemptions reflect the fact that, under the cross-guarantee provisions of the Federal Deposit Insurance Act, an insured depository institution is generally liable for any loss incurred by the FDIC in connection with the default of a commonly controlled depository institution. All transactions between a bank and its affiliates (including sister bank affiliates) are required, though, to be on terms and conditions that are consistent with safe and sound banking practices.²⁵ In addition, a bank may not purchase a low-quality asset from an affiliate (including a sister bank affiliate) unless the bank or its subsidiary, pursuant to an independent credit evaluation, committed itself to purchase such asset prior to the time such asset was acquired by the affiliate. Although a Federal Reserve official could not provide specific data on the number of insured holding company subsidiaries that qualify for the exemption, he estimated that more than 90 percent do so.

While Sections 23A and 23B and Regulation W impose few legal restrictions on holding companies selling assets among their insured depository subsidiaries for securing advances from different FHLBanks, there can be some bookkeeping and regulatory hurdles. Officials from one large thrift holding company with whom we spoke said that there are balance sheet management hurdles associated with the sale of assets from one subsidiary to another. For example, the officials said that asset sales may involve

²⁵ A Federal Reserve official stated that the Federal Reserve would interpret safe and sound banking practices to include that sales of assets between subsidiaries be conducted on market terms.

“de-pledging” assets pledged as collateral to secure advances at one FHLBank and pledge them to another FHLBank. Subsidiaries meeting the sister bank requirements must also ensure that the sale of assets meets bank regulatory agency capital requirements.²⁶ In addition, each FHLBank has established membership stock purchase requirements, which would require a subsidiary that received assets from an affiliate to purchase additional capital from the FHLBank. We note that the membership capital requirements for each FHLBank can differ.

We also note that it is difficult to determine the extent to which holding companies transfer assets between their subsidiaries and whether any such transfers result in competition between the FHLBanks. Federal Reserve officials said that they do not collect data on transfers of assets among subsidiaries, although one Federal Reserve official said that such transfers occur frequently. FHFB officials commented that it was not clear that holding companies had financial incentives to move collateral from one subsidiary to another to obtain favorable advance rates. The FHFB officials said that if a subsidiary had sufficient cash to purchase collateral from an affiliate, it already would have sufficient eligible collateral to secure advances from its local FHLBank and would not need additional collateral.

FHFB Has Not Identified Significant Advance Term Pricing Deficiencies, but FHLBank Safety and Soundness Data Reporting Can Be Improved

FHFB is responsible for helping ensure that the FHLBanks follow statutory and regulatory requirements in making advances and that competitive pressures within the FHLBank System do not compromise the System’s safety and soundness. Although the FHLBanks have adopted differing approaches to setting advance pricing terms, FHFB’s examination program has not identified significant violations in the banks’ practices over the past several years. However, as part of its oversight efforts, FHFB collects data on FHLBank collateral practices that have questionable value in their current format. In addition, FHFB does not collect data necessary to fully assess competition within the FHLBank System, such as data on the advance terms that holding company subsidiaries may receive from different FHLBanks. Such data would also help FHFB assess the potential risks associated with multidistrict membership.

²⁶ Banking regulators, such as FDIC, require insured depository institutions to meet leverage and risk-based capital requirements.

FHFB Examinations Have Not Identified Serious Advance Term Pricing Deficiencies

FHFB carries out its oversight responsibilities through, among other means, annual examinations and off-site monitoring. During the examination process, FHFB examiners review a range of activities at each FHLBank, such as its asset and liability management, collateral management practices, and compliance with relevant laws and regulations. Off-site monitoring is typically carried out by FHFB headquarters staff and involves the review of financial data that provides information and insights into the safety and soundness of the FHLBanks. Regular off-site monitoring between annual examinations is important because the FHLBanks' financial conditions and risks can change significantly in a short period. Off-site monitoring can help target examination reviews towards emerging risks at a particular FHLBank or across the System.

In reviewing advance pricing term compliance, FHFB examiners are responsible for determining whether the FHLBanks price their advances above the cost of issuing debt, the FHLBank's member products policy clearly outlines the standards and criteria for differential pricing, and the FHLBanks apply these standards and criteria consistently and without discrimination to all members. In reviewing collateral compliance, FHFB examination teams look at the policies the FHLBanks use to conduct their collateral verification site visits and the agreements they use to perfect their liens. FHFB examiners also review the procedures that the FHLBanks have established to ensure that they value their members' collateral frequently so that it is in line with the haircuts that they apply.

FHFB did not identify significant problems in the FHLBanks' advance term pricing practices in examinations completed in 2001 and 2002. FHFB officials said that their examinations have generally concluded that the FHLBanks comply with collateral requirements and setting advance interest rates. FHFB examinations completed between 2001 and 2002 that we reviewed identified no serious deficiencies.²⁷ According to FHFB examination criteria, a "violation" represents a significant deficiency at a FHLBank while a recommendation is less serious. With the exception of one violation for failure to perform advance collateral verification, FHFB examinations regarding collateral contained only recommendations that FHLBanks develop or expand policies. Similarly, according to the FHFB

²⁷An FHFB official provided us with copies of all examination reports for 2001 and 2002 that noted any findings related to collateral management practices.

officials, the agency has only recommended that certain FHLBanks describe more clearly their policies on differential advance term pricing.

FHFB's FHLBank System Safety and Soundness Data Reporting Procedures Have Limitations

Although FHFB has collected collateral data from the FHLBanks since 2000 that are intended to assist in monitoring the FHLBanks' safety and soundness, the data have questionable value in their current format. On an annual basis, FHFB has requested that the FHLBanks provide data on the level of collateral securing advances. FHFB requests data on, among other things, the total value of collateral securing advances, collateralization by member type (such as commercial bank and thrifts), collateralization by member size (such as members with \$10 billion or more in assets), and the use of eligible collateral by member institutions (such as the use of single-family mortgages and small business and agricultural CFI collateral). According to the FHFB's 2003 request letter, these data are "very valuable in exhibiting the System's safety and soundness and the extent to which traditional types of collateral secure advances." Additionally, FHFB stated in the letter that the information would help FHFB ascertain the acceptance and placement of small business and agricultural collateral by CFIs.

Although FHFB has identified such data as useful for assessing the FHLBank System's safety and soundness, we found that FHLBanks do not have clear information on how FHFB wants the data to be reported. Several FHLBanks that we visited report specific collateral—such as individual single-family mortgages or CFI loans—that has been pledged by their members to support outstanding advances. Officials at these FHLBanks said that they had provided the data in the format requested by FHFB. In contrast, other FHLBank officials told us that they reported all of the eligible collateral on the books of their members. A senior official from one of these FHLBanks said that since the bank has access to all the eligible collateral with whom it has blanket lien agreements, there was no need to report more specific loan-level data to FHFB. Officials from one FHLBank said that FHFB provided only general guidance on what collateral data to report, which required each FHLBank to develop its own reporting criteria.

Table 9 illustrates the differing approaches that the FHLBanks use to report collateral data to FHFB. The table shows the total advances outstanding, the reported collateral securing those advances, and the ratio of collateral to advances at each FHLBank as of December 31, 2002. The ratios at FHLBanks B and K show that their collateral to advance ratios are 1.23 to 1

and 1.26 to 1, respectively. These FHLBanks report to FHFB individual collateral securing advances. In contrast, FHLB E's ratio of 7.15 to 1 is explained by the fact that the bank reports to FHLBank the value of all the eligible collateral held by its members.

Table 9: FHFB Data on Collateralization and Advances as of December 31, 2002

Dollars in millions			
FHLBanks	Total collateral	Total advances	Collateralization ratio
Bank A	\$62,497	\$24,027	2.60
Bank B	\$30,297	\$24,651	1.23
Bank C	\$81,210	\$27,490	2.95
Bank D	\$158,553	\$77,205	2.05
Bank E	\$196,007	\$27,428	7.15
Bank F	\$77,510	\$25,991	2.98
Bank G	\$152,840	\$80,252	1.90
Bank H	\$62,294	\$23,044	2.70
Bank I	\$117,248	\$38,237	3.07
Bank J	\$113,604	\$66,017	1.72
Bank K	\$46,010	\$36,488	1.26
Bank L	\$55,041	\$19,686	2.80

Source: FHFB.

Note: The A-L listing of the FHLBanks in this table differs from the A-L listing in other tables in this report.

Because certain FHLBanks may report all of the eligible collateral held by their members, the data that FHFB receives on the acceptance and placement of CFI collateral—one of FHFB's stated reasons for collecting the data—is difficult to assess. As of December 31, 2002, the FHLBanks reported to FHFB that there was \$7.2 billion in small business and agricultural loans securing advances by CFIs. Of that \$7.2 billion figure, \$3.6 billion—or approximately 50 percent—was reported by one FHLBank, which reported the value of all the collateral on its members' books. This FHLBank reported the highest value of CFI collateral in the FHLBank System. However, an official from this FHLBank said that a small number of its members secured advances with CFI collateral and estimated that the total amount of such advances was \$25 million.

The Director of FHFB's Office of Supervision said that the agency planned to review its current collateral data collection and reporting procedures for

the FHLBanks. The Director said that the collateral data are currently used to complement FHFB's safety and soundness supervision program and that the data provided a broad overview of trends and anomalies. However, the Director also said that the collateral data did not substitute for FHFB's annual examinations at each FHLBank, which we discussed earlier. Although the FHLBank collateral data may provide some benefits for FHFB's examination program, FHFB's decision to review current reporting procedures appears to be appropriate. The current data do not allow for meaningful comparisons across the FHLBank System and the reported data on the placement of CFI collateral are potentially misleading. With better collateral data, FHFB's ability to monitor the FHLBank System's safety and soundness could be enhanced.

FHFB's oversight of the FHLBank System could also be enhanced by reviewing the extent to which competition may currently take place between FHLBanks and its potential effects on the System's safety and soundness. Available evidence suggests that competition may take place between the FHLBanks, including (1) key differences in advance term pricing across the FHLBank System, (2) statements by some FHLBank officials that holding company subsidiaries may play one FHLBank against another to obtain more favorable advance rates, and (3) the legal authority of holding company subsidiaries to transfer assets between one another thereby creating the potential that collateral may be moved from one subsidiary to another to obtain more favorable advance rates. Although there is evidence that competition between the FHLBanks takes place, the evidence is largely anecdotal and has not been quantified. Given FHFB's oversight responsibilities for the FHLBank System, it could benefit by collecting data necessary to better understand the degree of competition within the System. For example, FHFB could collect data on the advance terms—including interest rates—that the subsidiaries of holding companies obtain on advances and whether the eligible collateral at each subsidiary has fluctuated over time. By collecting such data, FHFB could identify the potential effects that holding company subsidiaries have on competition between the FHLBanks and whether such competition in any way has affected the FHLBanks' underwriting standards. Additionally, such data could assist FHFB in assessing the potential competitive and safety and soundness implications of multidistrict membership.

Conclusions

Within the framework established by statute and regulation, the FHLBanks have independent authority to set advance pricing terms that meet their business needs and the needs of their members. As a result, advance

pricing terms vary across the FHLBank System as evidenced by sometimes differing interest rates, tiered-pricing programs, collateral requirements, borrowing limits, and advance activity capital requirements. Because many holding companies have multiple subsidiaries, each of which may be eligible for membership in a different FHLBank, they have the opportunity to obtain advances from those FHLBanks that offer the most advantageous terms. Under exemptions to Sections 23A and 23B of the Federal Reserve Act, moreover, the potential also exists that holding companies can transfer assets from one subsidiary to another to obtain favorable advance pricing. These conditions create the potential for competition on advance pricing among the FHLBanks and any such pressures may be enhanced under multidistrict membership.

FHFB has a critical responsibility in helping to ensure that the FHLBanks sometimes differing advance pricing terms are conducted within statutory and regulatory requirements. In particular, FHFB is responsible for ensuring that the FHLBanks do not price advances below the cost of funds and fully secure advances with eligible forms of collateral. Although FHFB has not identified any serious violations in advance pricing terms in recent years, the agency has an important responsibility to ensure that any competitive pressures do not threaten the FHLBank System's safety and soundness. However, the data that FHFB currently collects on collateral from the FHLBanks is of questionable value in their current format for understanding the System's safety and soundness. Moreover, FHFB does not collect data that could be helpful in assessing the competitive implications of holding companies whose subsidiaries operate in different FHLBank districts as well as multidistrict membership.

Recommendations

To strengthen FHFB's safety and soundness oversight, we recommend that FHFB review its current collateral reporting requirements and work with the FHLBanks to obtain data that are useful in understanding collateral practices within the System. We also recommend that FHFB work with the FHLBanks to obtain data necessary to understand the competitive and safety and soundness implications of holding companies whose subsidiaries operate in different FHLBank districts as well as multidistrict membership.

Agency Comments and Our Evaluation

We received written comments on a draft of this report from FHFB and the Federal Home Loan Bank President's Conference, which are reprinted in appendixes III and IV, respectively. We also received technical comments from FHFB, several FHLBanks, and the Board of Governors of the Federal Reserve, which have been incorporated into the report where appropriate.

FHFB agreed to implement the recommendations contained in the report. FHFB stated that while the collateral data discussed in the report were used during the examination process, the data did not substitute for annual examinations. FHFB stated that it planned to examine the effectiveness of the collateral policies and procedures at each FHLBank and to identify practices, possibly to include enhanced data collection and reporting, to further the use of the most effective collateral practices. FHFB also stated that it planned to work with the FHLBanks to assess the value of additional data collection and reporting to monitor the competitive and safety and soundness influences of holding company subsidiaries that operate in multiple FHLBank districts. FHFB stated that its examinations have found that advance term pricing differed among the FHLBanks for many reasons, including the trade-offs between dividends and advance rates and competitive pressures. FHFB stated that it would be worthwhile to examine the extent to which competition—both between the FHLBanks and from the capital markets—can be a healthy influence on the efficient operation of the FHLBanks.

The FHLBank President's Conference stated that the report correctly noted that the advance pricing and collateral practices of the 12 FHLBanks differ. The Conference stated that the FHLBank Act and FHFB regulations establish a framework in which individual FHLBanks can establish policies that meet the needs of their member institutions. The Conference also stated that statutory and regulatory provisions that require advance interest rates to be set above borrowing costs and advances to be secured by eligible collateral ensure that the FHLBanks operate in a safe and sound manner. The Conference also stated that its members were prepared to work with FHFB to collect data necessary to understand the collateral practices across the FHLBanks.

As agreed with your offices, unless you publicly announce the contents of this report earlier, we plan no further distribution until 30 days from the report date. At that time, we will send copies of this report to the Chairman of the Senate Committee on Banking, Housing, and Urban Affairs; and the

Ranking Member of the Subcommittee on Capital Markets, Insurance, and Government Sponsored Enterprises of the House Committee on Financial Services. We will also send copies to FHFB, the FHLBank President's Conference, the FHLBanks, and the Board of Governors of the Federal Reserve. We will also send copies to others upon request. In addition, this report will be available at no charge on GAO's Web site at <http://www.gao.gov>. Please contact Mr. Wesley M. Phillips or me at (202) 512-8678, or email (phillipsw@gao.gov or shearw@gao.gov) if you or your staff have any questions concerning this report. GAO staff who made major contributions to this report are listed in appendix V.



William B. Shear
Director, Financial Markets
and Community Investment

Objectives, Scope, and Methodology

As discussed with your staff, our report objectives are to (1) describe the laws and regulations pertaining to the terms that FHLBanks can offer on advances; (2) provide information on whether key differences exist in current advance pricing and other terms across the FHLBanks; (3) determine whether holding companies face any legal or regulatory barriers in transferring assets among subsidiaries who are members of different FHLBank districts; and (4) describe FHFB's safety and soundness oversight of the FHLBanks' advance pricing practices and review selected data that FHFB collects to monitor the safety and soundness of the FHLBank System.

To meet objective (1), we reviewed the Federal Home Loan Bank Act as amended. We also reviewed the FHFB regulations that govern or describe the terms that FHLBanks can offer on advances. We interviewed FHFB and FHLBank officials to obtain their views on the terms FHLBanks can offer on advances.

To meet objective (2), we interviewed FHFB, the 12 FHLBank presidents, credit staff from 7 of the 12 FHLBanks, and we sent a structured questionnaire to each of the 12 FHLBanks and received responses from each of the banks. Additionally, we reviewed the credit policies of each of the 12 FHLBanks and reviewed data on advance interest rates for those FHLBanks that post such data on their Web sites. We note that the data posted on the FHLBank Web sites are subject to change and that the actual rates members actually pay may differ due to advance term negotiations between FHLBanks and their members. Two other FHLBanks separately provided their advance rates for the dates that we used. With this information, we compared advance pricing and other terms across the FHLBanks to identify key differences. The scope of our work did not involve developing a methodology to determine why individual FHLBanks charge the advance interest rates or other advance pricing terms that they do.

To meet objective (3), we reviewed applicable laws and regulations regarding the transfer of funds and assets among holding companies and their subsidiaries, including the Federal Reserve Act, Federal Home Loan Bank Act, Home Owners' Loan Act, FHFB regulations, and Federal Reserve Board regulations. We also interviewed representatives from the Federal Reserve Board, FHFB and a large holding company.

To meet objective (4), we interviewed FHFB officials, reviewed FHFB's advance pricing examination guidelines, and reviewed selected

examination reports for 2001 and 2002 related to advance pricing and collateral requirements. We did not evaluate the effectiveness of FHFB's examination program. To assess FHFB's collateral data reporting process, we reviewed FHFB's data request forms and the data provided by the FHLBanks. We also interviewed officials at selected FHLBanks to determine their approach to reporting the collateral and other data and we interviewed FHFB officials on these issues.

We conducted our review from January to September 2003 in Washington, D.C.; New York, New York; Topeka, Kansas; Dallas, Texas; Atlanta, Georgia; and Pittsburgh, Pennsylvania, and Indianapolis, Indiana, in accordance with generally accepted government auditing standards.

Advance Interest Rates Charged by Specific FHLBanks on Selected Dates

Table 10: Comparison of Selected FHLBank Interest Rates on Fixed Rate Advances (July 18, 2003)^a

Term	Bank A	Bank B	Bank C	Bank D	Bank E	Bank F	Bank G	Bank H	Bank I	Bank J	Bank K	Range	Difference in basis points
12 mo.	1.29	1.20	1.54	1.53	1.22	1.41	1.45	1.23	1.34	1.43	1.38	1.20-1.54	34
24 mo.	1.77	1.68	1.95	1.95	1.74	1.84	1.98	1.76	1.86	1.84	1.96	1.68-1.98	30
36 mo.	2.31	2.28	2.5	2.48	2.32	2.42	2.51	2.31	2.46	2.48	2.5	2.28-2.51	23
48 mo.	2.83	2.80	3.12	3.00	2.93	2.92	3.09	2.84	2.98	3.01	3.04	2.80-3.12	32
60 mo.	3.27	3.22	3.4	3.43	3.34	3.34	3.48	3.28	3.39	3.45	3.46	3.22-3.48	26

Source: Selected FHLBanks.

Note: The A-K listing of the FHLBanks for this table differs from the alphabetic listings in other tables in this report.

^aThe interest rates shown are generally for regular fixed term and rate advances with no discounting. The FHLBanks also differ in their policies regarding payment frequency and daycount accrual methods. No attempt is made here to harmonize the data to a single payment frequency and daycount accrual standard.

Table 11: Comparison of Selected FHLBank Interest Rates on Fixed Rate Advances (July 25, 2003)^a

Term	Bank A	Bank B	Bank C	Bank D	Bank E	Bank F	Bank G	Bank H	Bank I	Bank J	Bank K	Range	Difference in basis points
12 mo.	1.26	1.56	1.36	1.45	1.55	1.40	1.40	1.21	1.30	1.44	1.24	1.21-1.56	35
24 mo.	1.78	1.97	1.85	1.96	1.96	1.94	1.84	1.73	1.80	1.84	1.78	1.73 -1.97	24
36 mo.	2.35	2.57	2.52	2.61	2.43	2.58	2.50	2.39	2.41	2.54	2.39	2.35-2.61	26
48 mo.	3.02	3.15	3.12	3.24	3.18	3.18	3.06	2.99	3.01	3.15	2.99	2.99-3.24	25
60 mo.	3.48	3.64	3.61	3.69	3.54	3.66	3.51	3.46	3.49	3.65	3.47	3.46-3.69	23

Source: Selected FHLBanks.

Note: The A-K listing of the FHLBanks for this table differs from the alphabetic listings in other tables in this report.

^aThe interest rates shown are generally for regular fixed term and rate advances with no discounting. The FHLBanks also differ in their policies regarding payment frequency and daycount accrual methods. No attempt is made here to harmonize the data to a single payment frequency and daycount accrual standard.

Comments from the Federal Housing Finance Board



Federal Housing Finance Board

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August 27, 2003

Mr. Thomas J. McCool
Managing Director
Financial Markets and Community Investment
U. S. General Accounting Office
Washington, DC 20548

Dear Mr. McCool:

This letter represents the response of the Federal Housing Finance Board (the "Finance Board") to the General Accounting Office's draft report, "Key Loan Pricing Terms Can Differ Significantly" (the "Draft Report"). The Draft Report makes two recommendations regarding collateral reporting requirements and the collection of data on holding companies. We appreciate your recommendations and will carefully consider how to improve data collection in those areas. In addition, we have a few specific comments on your two recommendations, which supplement the technical comments we provided orally to your representatives during a meeting on August 20, 2003.

First, the Draft Report observes that there is some confusion among the FHLBanks regarding data on collateral securing advances that they must report to the Finance Board. The Draft Report recommends, therefore, that the Finance Board review the effectiveness of its current collateral data collection program and obtain additional data that would be useful in assessing collateral practices within the system. In response to your recommendation, we intend to further examine the effectiveness of the collateral policies and procedures at each of the FHLBanks and to identify practices, possibly to include enhanced data collection or reporting, to further the use of the most effective collateral policies and procedures at each of the FHLBanks.

We currently use the collateral data collection instrument referred to in the Draft Report to complement our safety and soundness supervision. The data provide a broad view of trends and anomalies. However, such data do not substitute for a thorough review of collateral practices conducted by Finance Board examination staff. Our examiners conduct such reviews by assessing each FHLBank's collateral policies and procedures and reviewing the FHLBank's practices in monitoring its own compliance with those policies and procedures. More specifically, our examiners review data on

Appendix III
Comments from the Federal Housing Finance
Board

collateral delinquencies, credit ratings, and delivery status, and monitor the frequency of on-site reviews of members' collateral by FHLBank staff.

Second, the Draft Report recommends that the Finance Board work with the FHLBanks to collect data, such as on the differences in advance pricing by FHLBanks, that are necessary to monitor the competitive and safety and soundness implications of holding companies whose subsidiaries operate in multiple FHLBank districts. In response to your recommendation, we will work with the FHLBanks to assess the value of additional data collection and reporting to monitor the competitive and safety and soundness influence of holding companies whose members operate in multiple FHLBank districts, taking into account the possible effect on advance pricing of outside, as well as inside, competitive influences on the FHLBanks.

Finance Board examiners currently review FHLBank advance pricing policies, assess their consistency with the FHLBank's profit or net income goals, and check for compliance with statutory and regulatory requirements that pricing be both above cost and non-discriminatory among members. On the basis of those examinations, we have found that advance prices among the FHLBanks differ for many reasons, including decisions made by the cooperative members of each FHLBank as to their preferences with respect to the trade-offs between advance pricing and dividends. We have also observed that competitive pressures from capital markets generally can and do influence the advance prices charged by individual FHLBanks. As such, an area worthy of inquiry is the extent to which competition, both among the FHLBanks and between the FHLBanks and other capital market entities, can be a healthy influence on the efficient operation of the FHLBanks.

We appreciate the issues raised in the Draft Report and the opportunity to respond to your analysis, both by this letter and in our previous discussions with your staff. Thank you again for the high-quality professional effort of your team.

Sincerely,



Stephen M. Cross
Director
Office of Supervision

Comments from the Federal Home Loan Bank Presidents' Conference



MICHAEL A. JESSEE
President and Chief Executive Officer
michael.jessee@fhlbboston.com

August 27, 2003

Wesley Phillips
Assistant Director
U.S. General Accounting Office
Washington, DC 20548

Dear Mr. Phillips:

On behalf of the Federal Home Loan Bank Presidents' Conference, I am pleased to submit this comment letter on the report entitled *Federal Home Loan Bank System: Key Loan Pricing Terms Can Differ Significantly* (GAO-03-973).

Several of the Federal Home Loan Banks (FHLBanks) have already provided the General Accounting Office (GAO) with technical comments on the draft. The intent of this letter is to address the general nature of the report.

The report correctly notes that advances-pricing and collateral practices differ among the 12 FHLBanks. The FHLBank Act and Federal Housing Finance Board (FHFB) regulations establish a framework within which the board of directors of an FHLBank can approve an advances-pricing policy that best satisfies the needs of that FHLBank's member institutions. Statutory and regulatory provisions require that advances rates be set above all-in borrowing costs and that advances be fully secured by eligible collateral. Thus, each FHLBank makes advances in a safe and sound manner while meeting the needs of its member institutions and the communities they serve.

The FHLBanks are prepared to work with the FHFB should it decide to expand its data collection to better understand the collateral practices across the 12 FHLBanks.

Sincerely,

A handwritten signature in black ink, appearing to read "Michael A. Jessee".

Michael A. Jessee
Chairman, Research and Planning Committee
Federal Home Loan Bank Presidents' Conference

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Acknowledgments

In addition to the individuals named above, Tanya Cruz, Crystal Daniels, Rachel DeMarcus, M’Baye Diagne, Marc Molino, Andy Pauline, Mitchell B. Rachlis, and Barbara Roesmann made key contributions to this report.

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